



Jack Hillier
Markets Policy
Strategy & Competition Division
Financial Conduct Authority
12 Endeavour Square
London
E20 1JN

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Dear Mr. Hillier,

Joint Trade Association letter regarding the reporting of commodities transactions and ESMA Guidelines for Reporting under Articles 4 and 12 of SFTR

This letter is to follow up on our 13 February 2020 meeting with you and your FCA colleagues (Paul Willis and Carmel Deenmamode) to discuss the reporting obligation in the Securities Financing Transaction Regulation (Regulation (EU) 2015/2365) (SFTR) and the associated technical standards for reporting rules under SFTR¹.

On behalf of the individual members of the Joint Trade Associations², representing the commodities trading industry, we would like to thank you for your engagement in the issues discussed. As an industry we have been grappling with the challenges inherent in reporting commodities transactions under SFTR for some time now, as you know.

We welcome the publication by ESMA on 6 January 2020 of the Final Report on Guidelines on Reporting under Articles 4 and 12 of SFTR, and the Guidelines themselves on that same date.

In particular, we welcome the statement in: Section 3.1.1.8 of ESMA's Guidelines that "Commodities transactions entered into for operational and/or industrial purposes which are clearly not for financing purposes, i.e. are concluded for commercial purposes, do not contribute to the systemic risk addressed by SFTR. Therefore, these market transactions should not fall under the definition of an SFT and therefore should not be reported under SFTR."

While it is helpful clarification that ESMA views these types of transactions as out of scope, it is introduced at a late stage in the implementation timeframe along with ESMA's Guidelines document at 215 pages, leaving only 12 weeks to the 11 April application date.

Even though ESMA provides some guidance in Section 3.1.2.2 of ESMA's Guidelines that "Clarification on the exclusion of (i) Commodity transactions entered into for reasons other than

¹ Commission Delegated Regulation (EU) 2019/356 and Commission Implementing Regulation (EU) 2019/363.

² The Joint Associations are GFMA, LBMA, FIA, EFET [and CMCE]. More information about each organization is included in the Annex.



financing, such as for transportation and capacity needs and for operational purposes; (ii) Transactions entered into for gas storage purposes based on market practice/industry standards and including a sell/buy-back or BSB obligation; and (iii) Transactions whereby the quantity/ characteristics of the commodity to be repurchased are materially different compared to the quantity/ characteristics of the commodity sold, as all these transactions are not in scope of SFTR reporting;”, the ‘purpose test’ clarification requires firms to engage with their counterparties and then to implement system changes that will enable these transactions to be excluded from reporting which is further complicated by the fact that the reporting obligation does not apply to NFCs before 10 January 2021.

Since 6 January, financial institutions have been looking at how to operationalise this clarification, which starts with examining the business activity of their counterparty for every transaction. The changes required include looking at the contractual documentation between the parties and deciding whether/how to incorporate a new representation from a corporate client that all transactions entered into through the contractual relationship are in fact for operational and/or industrial purposes, unless the client notifies the financial institution otherwise. As we explained at the meeting, it is anticipated that a mechanism must be put in place, both contractually and from an IT perspective, for circumstances where the corporate client determines that a particular transaction does not meet the operational and/or industrial purpose test, even though it is subject to the same [master] terms as other transactions with the same counterparty which do meet the test.

Linkage between opening and closing leg of transactions

As we discussed at the 13th February meeting, the industry is also working through the clarification set out in ESMA’s Final Report and Guidance on the nature of the linkage between an opening and closing leg of a transaction in order for it to be in scope under SFTR. We refer to Paragraph 14(c) and Paragraph 88 of the Final Report and to Section 4.2.6 of the Guidelines. Our members are working hard to operationalise the reporting of these transactions, however we believe further guidance may be helpful for certain transaction types. We will provide additional detail/use case examples as soon as possible. We set out some key issues below.

Multiple UTIs - the two-legged commodities transactions referred to above are executed, confirmed and booked as separate transactions, typically under an ISDA (or similar) Master Agreement. The SFTR reporting templates assume a single SFT, critically with one UTI, whereas the aforementioned commodities transactions consist of two separate UTIs.

Collateral - if entered into pursuant to an ISDA (or similar) master agreement the two linked transactions may be collateralised as part of a wider trading portfolio. It is not possible to isolate and report the collateral position relative to specific SFTs within a portfolio.

Valuation - similarly the requirement to report linked transactions as a single SFT also gives rise to complications on calculating Valuation data. Reporting assumes a single value for an SFT for a



given date, whereas the underlying IT systems will hold data for both commodities transactions; rules for combining data to report as a single SFT value is unclear.

The commodities industry therefore requires specific guidance on how to report two linked transactions as one SFT and how to report the associated collateral position within a trading portfolio and expectation for valuation data.

Risk of over/under-reporting from 11 April 2020

We are concerned that given the relatively short timeframe to implement a reporting solution further to ESMA's Guidelines, firms may initially report transactions that are not in fact in scope for SFTR due to the 'operational and/or industrial purposes' clarification. Furthermore, the risk of under-reporting persists due to the ambiguity on linked transactions and challenges with reporting two trades as a single SFT, resulting in neither being reported at go-live.

We would respectfully request that FCA not prioritise supervisory action against counterparties that over/under-report transactions under SFTR, giving firms a reasonable amount of time to address the challenges we have discussed above, and described in detail at our 13 February meeting.

We would welcome the opportunity to discuss this issue with you and are also very happy to answer any questions you may have in the meantime.

Yours sincerely,

Sean Barwick, GFMA
Sean.Barwick@afme.eu

Sakhila Mirza, LBMA
Sakhila.Mirza@lbma.org.uk

Karl-Peter Horstmann, EFET
karl-peter.horstmann@rwe.com

Christiane Leuthier, FIA
cleuthier@fia.org

Samina Anwar, CMCE
Samina.Anwar@cargill.com



Annex 1 – Information about Signatory Organisations

About GFMA:

The Commodities Working Group of GFMA focuses on regulatory issues specific to banks operating in the financial and physical commodities markets. The CWG's work centers around the creation of a more level regulatory playing field for the commodity markets, advocating consistency and avoiding duplication among legislative measures.

The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, visit <http://www.gfma.org>

About LBMA:

The London Bullion Market Association (LBMA) is an independent market association representing the global markets for gold, silver, platinum and palladium. Participants in these markets include financial institutions, central banks, refiners, mining companies, mints, traders, transporters and security companies. LBMA represents 143 companies active in the precious metals markets in over 30 countries. LBMA is focused on adding value to the global precious metals industry by setting standards and developing market services, thereby ensuring the highest levels of integrity, transparency and quality.

LBMA's Regulatory Affairs Committee (RAC) comprises legal and compliance representatives from financial institutions. The RAC monitors and analyses information concerning international regulation affecting the precious metals market, and recommends possible actions that LBMA may take in response to proposed or upcoming regulation. For more information, visit <http://www.lbma.org.uk>.

About EFET:

The European Federation of Energy Traders (EFET) promotes competition, transparency and open access in the European energy sector. We build trust in power and gas markets across Europe, so that they may underpin a sustainable and secure energy supply and a competitive economy.

We do this by:

- Working to improve the functionality and design of European gas, electricity and associated markets for the benefit of the overall economy, society and especially end consumers.
- Developing and maintaining standard wholesale supply contracts and standardising related transaction and business processes.



- Facilitating debate amongst TSOs, regulators, policy makers, traders and others in the value chain about the future of the European energy market.

About FIA:

FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in London, Singapore and Washington, D.C. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from more than 48 countries as well as technology vendors, lawyers and other professionals serving the industry.

About CMCE:

Commodity Markets Council Europe (CMCE) is the only association in Europe representing the range of commodity market participants - agriculture, energy, metals and other commodity market participants, benchmark providers, price reporting agencies, and trading venues operating in the EU, EEA, Switzerland and neighbouring countries. The majority of CMCE members use commodity derivative markets to hedge the risks related to their physical activities and assets. CMCE's key purpose is to engage with policymakers and regulators to promote liquid and well-functioning commodity derivative markets in Europe.